

REVISED OPEN MEETING**MEMORANDUM**

TO: THE COMMISSION

FROM: Utilities Division

DATE: October 24, 2019

RE: IN THE MATTER OF THE APPLICATION OF ARIZONA PUBLIC SERVICE COMPANY TO IMPLEMENT A TAX EXPENSE ADJUSTOR MECHANISM (DOCKET NO. E-01345A-18-0003).

SUBJECT: TAX EXPENSE ADJUSTOR MECHANISM PHASE III

INTRODUCTION

Enclosed are the Commission Staff's memorandum and proposed order for the Matter of the Application of Arizona Public Service Company to Implement a Tax Expense Adjustor Mechanism (Docket No. E-01345A-18-0003). This is only a Staff recommendation to the Commission; it has not yet become an order of the Commission. The Commission may accept, amend or reject Staff's proposed order.

You may file comments to the recommendation(s) of the proposed order by filing an original and thirteen (13) copies of the comments with the Commission's Docket Control Center at 1200 West Washington Street, Phoenix, Arizona 85007 by 4:00 p.m. on or before **October 28, 2019**.

This matter may be scheduled for Commission deliberation at its Open Meeting scheduled **October 29, 2019, at 10:00 a.m.**

If you have any questions about this matter, please contact Alexander Ibhadé Igwe of our Staff at (602) 542-1331, or Elijah Abinah, Director, at (602) 542-6935.

BACKGROUND

Arizona Public Service Company ("APS" or "Company") is a public utility corporation certificated to provide electric service in the state of Arizona.

On April 10, 2019, APS filed its second supplemental application for Commission approval to implement the Tax Expense Adjustor Mechanism ("TEAM") Phase III, along with certain modifications to its TEAM Plan of Administration ("POA"). On August 29, 2019, Staff docketed a memorandum and proposed order recommending Commission approval of the APS Phase III

filing, with certain modifications related to the tax savings associated with protected Excess Deferred Income Taxes ("EDIT") from January 1, 2018 through September 30, 2019. In that filing, Staff noted that APS did not propose any mechanism to refund accrued tax savings over the above referenced period. As a result, Staff recommended that the Commission order APS to implement a one-time bill credit that refunds approximately \$60 million of tax savings to its ratepayers. On October 22, 2019, APS met with Staff to discuss its revised proposal regarding tax savings related to protected EDIT over three years (January 1, 2018 through December 31, 2020), with emphasis on amortization over the last twenty-two months. This memorandum and proposed order reflect Staff's modification to its original recommendations in this proceeding.

The Commission approved a TEAM and the related POA for APS in Decision No. 76295, dated August 18, 2017. APS' TEAM and POA were approved in anticipation of the enactment of the 2017 Tax Cuts and Jobs Act ("Tax Act" or "TCJA"), which became effective January 1, 2018. The Tax Act resulted in several changes to the federal tax laws, amongst which was a reduction of the Federal Corporate Income Tax Rate ("FIT") from the highest rate of thirty-five percent to a flat rate of twenty-one percent. This provision impacted most utility companies' revenue requirement; by decreasing federal corporate income tax expense, Accumulated Deferred Income Taxes ("ADIT") and the related EDIT, amongst other cost elements.

On January 8, 2018, APS filed an application for Commission approval to implement TEAM Phase I, which accounted for reduction of FIT from the highest rate of thirty-five percent to a flat rate of twenty-one percent. APS reported that the impact of change in FIT resulted in a decrease of \$119.074 million to its authorized revenue requirement. On March 5, 2018, the Commission, in Decision No. 76601, approved Staff's recommendation to authorize APS to refund its tax savings of \$119.074 million through a monthly bill credit of \$0.004912 per Kilowatt Hour ("kWh") to most of its customers.

On August 13, 2018, APS filed a supplemental application for Commission approval to implement TEAM Phase II related to the impacts of the Tax Act on its unprotected ADIT. APS stated that implementation of the Tax Act resulted in approximately \$86.5 million of jurisdictional unprotected EDIT. The Company requested that the Commission authorize it to refund the entire savings over twelve months. Second, the Company requested Commission approval to change its existing TEAM Phase I bill credit rate, from \$0.004912 per kWh to \$0.004194 per kWh. Finally, APS requested certain modifications to its TEAM POA. On March 19, 2019, the Commission, in Decision No. 77139, approved APS TEAM Phase II, as well as its requested modifications to both the TEAM Phase I bill credit rate and the TEAM POA.

THE COMPANY'S SUPPLEMENTAL PROPOSALS

On April 10, 2019, APS filed its second supplemental application for Commission approval to implement TEAM Phase III, along with certain modifications to its TEAM POA. The Company reports that implementation of the Tax Act resulted in approximately \$881 million of jurisdictional protected EDIT. APS proposes to amortize its reported \$881 million of protected EDIT over 28.5 years, based on the Reverse South Georgia Method ("RSGM"). The Company estimates an annual amortization of \$31 million of protected EDIT; and a decrease of \$34.452 million in revenue

requirement, due to the impacts of gross revenue conversion factor and pertinent adjustments to rate base.

APS seeks Commission approval to refund \$103.5 million of savings related to protected EDIT from January 1, 2018 through December 31, 2020, in this proceeding. The Company states that its proposal is predicated on the assumption that the impacts of the Tax Act will be fully evaluated and incorporated in rates approved in the next rate case, to be filed by October 31, 2019. APS requests Commission approval to refund \$64 million of the above savings as a one-time bill credit, to account for savings accrued over twenty-two months, from January 1, 2018 through October 31, 2019. The Company proposes to refund its estimated savings of \$64 million as a one-time bill credit at the rate of \$0.006945 per kWh, to customers of record between August 1, 2019 and October 31, 2019. In other words, APS proposes to refund each customer of record, an amount equal to the product of total consumption between August and October 2019 (three months) multiplied by \$0.006945 per kWh. APS argues that the proposal to refund its tax savings to only customers of record, between August and October 2019 (three months), is a practical approach because of the complexity associated with tracking and refunding all its customers over the last twenty-two months (January 1, 2018 through October 31, 2019). In order to allow for adequate time to set-up a mechanism to refund its savings, APS requests that the Commission authorize it to implement its one-time bill credit in the first billing cycle of December 2019. The Company proposes to maintain a true-up mechanism that accounts for over/under refunded savings for future consideration, in the event that it cannot locate all customers of record between August and October 2019.

APS also proposes to account for approximately \$39.5 million of protected EDIT savings from November 1, 2019 through December 31, 2020, through a monthly bill credit rate of \$0.001169 per kWh. The Company proposes to implement its first monthly bill credit in December 2019, for ease of administration. APS states that in the event that all savings related to the Tax Act are not fully incorporated in the rates approved in its new rate case, it will file a new TEAM to address the impacts of the Tax Act from January 1, 2021, subsequent to a Commission decision in its next rate case filing.

Normalization Rules related to Protected ADIT

APS acknowledges that under the Internal Revenue Service ("IRS") normalization rules, Section 1561(d)(3)(B) of the Internal Revenue Code ("Code") prescribes the Average Rate Assumption Method ("ARAM") as the default method for amortizing protected EDIT. The Company states that under certain conditions and subject to IRS approval, the IRS permits adoption of an alternate method known as the RSGM for amortizing protected EDIT. The IRS permits adoption of the RSGM if a utility does not have adequate records to support the use of ARAM. APS states that its adoption of the RSGM in this proceeding is appropriate because it lacks the requisite records to support application of ARAM. APS contends that it satisfies the conditions specified for adopting the RSGM under the Tax Act. The Company argues that its proposal to adopt the RSGM is reasonable because it would be cost prohibitive to recreate the required records to amortize its protected EDIT based on ARAM. Finally, APS claims that its

adoption of the RSGM is beneficial to ratepayers, since it more ratably amortizes protected EDIT over the remaining life of the related regulatory assets.

APS has provided additional justification for its proposed adoption of the RSGM in this proceeding. The Company, in its response to Staff's second set of data requests, stated that Section 13001(d)(2) of the Tax Act provides "that if, as of the first day of the taxable year that includes the date of enactment of the TCJA, the taxpayer was required by a regulatory agency to compute depreciation for public utility property on the basis of an average life or composite rate method, and the taxpayer's books and underlying records did not contain the vintage account data necessary to apply ARAM, the taxpayer will be treated as using a normalization method of accounting if, with respect to such jurisdiction, the taxpayer uses RSGM for public utility property that is subject to the regulatory authority of that jurisdiction." APS contends that because its books and the underlying records do not contain vintage account data required for ARAM and it was required by the Commission to compute depreciation on its regulated utility property based on an average life or composite rate method, its proposal to adopt the RSGM is appropriate and consistent with Section 13001(d)(2) of the Tax Act.

APS recognizes that adoption of the RSGM is subject to IRS approval for compliance with the normalization rules, and that there are severe penalties associated with violation of the IRS normalization rules related to protected EDIT. As a result, APS, in conjunction with its Tax Accountants, PricewaterhouseCoopers, LLP, have been engaged in preliminary discussions with IRS for issuance of a Private Letter Ruling ("PLR"), to affirm if APS's adoption of the RSGM is consistent with the provisions of Section 168(i)(9) of the Code. APS reports that on May 15, 2019, the IRS responded to its pre-submission conference for a PLR, indicating that it was unable to issue the requested ruling. The IRS stated in its response to APS that "The situation presented in the request is generally the subject of ongoing consideration for published guidance regarding the treatment of excess deferred taxes under the normalization rules and sound tax administration dictates that we refrain from issuing rulings on this matter until the broader questions considered in the guidance project are resolved. Therefore, we decline to issue the requested ruling."

APS continues to argue that its decision to refund tax savings related to protected EDIT before obtaining a PLR is in the public interest. The Company contends that this filing is predicated on its desire to timely refund all tax savings associated with the Tax Act to the ratepayers. The Company further contends that this filing is prudent and beneficial to ratepayers due to the uncertainties surrounding when the IRS might issue its suggested guidance and/or issue a PLR. APS states that if the IRS determines that its adoption of the RSGM in this proceeding is inconsistent with the normalization rules, it will recalculate both its proposed protected EDIT amortization based on ARAM as well as the related bill credit rate, to address any variance with the use of the RSGM. APS states that if it becomes necessary to revise its protected EDIT based on ARAM, the Company will record any under recovery as a regulatory asset for future recovery in a subsequent filing or as a part of its next rate case.

Reconciliation with APS's 2017 Tax Return

APS reports that there were variances between its accounting records and federal income tax positions on protected and unprotected EDIT for the financial year ended December 31, 2017. The variances resulted in an excess protected EDIT of \$8.151 million and a negative unprotected EDIT balance of \$2.626 million, for a net EDIT of \$5.525 million. APS proposes to record the net reconciliation amount of \$5.525 million as part of its protected excess tax regulatory liability and amortize it over 28.5 years, consistent with its proposal under the RSGM.

Change to the TEAM POA

In this proceeding, APS has modified its TEAM POA to reflect changes ordered by Decision Nos. 76601 and 77139. The Company also seeks Commission approval to modify its TEAM POA to include the option to hold any under/over-refunded amounts in a balancing account until its next general rate case, in lieu of an annual adjustment.

STAFF ANALYSIS AND RECOMMENDATIONS

Staff has reviewed APS's second supplemental application for Commission approval to refund approximately \$881 million of tax savings related to protected EDIT over 28.5 years pursuant to the RSGM. Staff also reviewed the Company's related proposal to refund approximately \$103.5 million to account for savings associated with protected EDIT, from January 1, 2018 through December 31, 2020. Further, Staff evaluated APS's revised proposal to refund \$64 million of savings accrued between January 1, 2018 and October 31, 2019, as a one-time bill credit at the rate of \$0.006945 per kWh, to customers of record between August 1, 2019 and October 31, 2019. In addition, Staff evaluated the Company's proposal to refund \$39.5 million of protected EDIT savings, from November 1, 2019 through December 2020, as a monthly bill credit at the rate of \$0.001169 per kWh. Finally, Staff reviewed the APS proposed modifications to its TEAM POA.

Staff determined that APS' proposal to refund \$64 million of protected EDIT accrued from January 1, 2018 through October 1, 2019 as a one-time bill credit, at the rate of \$0.006945 per kWh, to customers of record between August 1, 2019 and October 31, 2019, is reasonable. Although Staff would have preferred that the benefits of the Tax Act inure to all customers from January 1, 2018 to date, APS's contention that it would be impractical to track and refund all customers due to associated costs and customer attrition, is logical and persuasive. Staff finds that it is appropriate to accept the Company's one-time bill credit rate of \$0.006945 per kWh, derived as a product of \$64 million divided by estimated total consumption of 9,205,638,162 kWh (August 1, 2019 and October 31, 2019). Staff also recommends Commission approval of the Company's monthly bill credit rate of \$0.001169 per kWh, calculated based on \$39.5 million divided by total estimated consumption of 33,728,949,000 kWh, from November 1, 2019 through December 31, 2020. Staff concurs with APS's assumption that the impacts of the Tax Act will be fully incorporated in its next rate case. Although Staff believes that the full impacts of the Tax Act will be reflected in APS's next rate case, the Company's proposal to maintain a true-up mechanism and file a TEAM to account for savings from January 1, 2021, is reasonable.

Staff understands that the IRS normalization rules require utilities to adopt the ARAM as the default methodology for amortizing protected EDIT. Staff is equally aware that the IRS Code and certain provisions of the Tax Act allow utilities to adopt the RSGM, if certain conditions exist. Staff is also cognizant of APS's concerted efforts to obtain a PLR from the IRS to affirm that its adoption of the RSGM is consistent with the IRS normalization rules. The correspondence from the IRS to APS confirms IRS' unwillingness to issue a PLR on this matter, prior to issuance of its proposed guidance on the impact of the Tax Act of protected EDIT. Finally, Staff finds that APS's proposal to revise its protected EDIT amortization based on the ARAM, if the IRS determines that the adoption of the RSGM is inconsistent with the normalization rules; and account for any variance within the context of its next rate case or in a subsequent filing, is reasonable. APS's proposal to duly account for any variance between adoption of the RSGM and ARAM, and appropriately account for any variance will ensure that the full benefits of its tax savings related to protected EDIT will ultimately inure to the ratepayers. Based on these facts and APS's desire to timely refund all savings related to the Tax Act to its ratepayers, Staff finds that it is in the public interest for the Commission to authorize APS to refund \$881 million of protected EDIT based on the RSGM over 28.5 years. Staff further recommends that the Commission order APS to file a copy of an IRS ruling or determination related to its adoption of the RSGM in this docket, no later than within thirty days of receiving the related IRS notice. Staff further recommends that the Commission order APS to file necessary revisions to its proposal in this proceeding and propose a mechanism for addressing any variance if the IRS determines that adoption of the RSGM for amortizing protected EDIT as approved by the Commission in this proceeding does not conform with IRS normalization rules. Staff further recommends that the Commission order APS to provide a detailed analysis regarding the jurisdictional impact of the Tax Act on its operations in Arizona, for a comprehensive evaluation within the context of its next rate case which is due to be filed on October 31, 2019.

APS Proposed Changes to TEAM POA

Staff has reviewed APS's proposed revisions to its existing TEAM POA, to incorporate changes ordered by Decision Nos. 76601 and 77139. Staff also reviewed the Company's proposal to modify its POA to reflect the option to hold any over/under refunded amounts in a balancing account for consideration and approval in its next rate case, in lieu of filing an annual adjustment report. Staff finds APS's proposed modifications to be consistent with Commission Decision Nos. 76601 and 77139. Staff also finds that APS's proposal to defer any variance related to the Tax Act for consideration within the context of the next rate case is appropriate. Staff recommends Commission approval of APS's proposed modifications to its TEAM POA.

Compliance Filings

Staff recommends that the Commission order APS to file a copy of the IRS ruling or determination related to its adoption of the RSGM in this docket, no later than within thirty days of receiving the related IRS notice.

THE COMMISSION

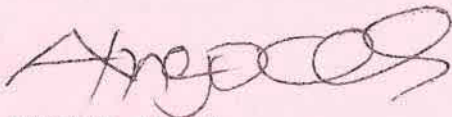
October 24, 2019

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Staff recommends that the Commission order APS to file necessary revisions to its proposal in this proceeding as well as propose a mechanism for addressing any variance, if the IRS determines that adoption of the RSGM for amortizing protected EDIT, as approved by the Commission in this proceeding, does not conform with IRS normalization rules, within thirty days of an IRS notice or ruling.

Staff recommends that the Commission order APS to provide a detailed analysis regarding the jurisdictional impact of the Tax Act on its operations in Arizona for a comprehensive evaluation in its next rate case, within 180 days of a Commission decision in this docket.

Staff recommends that the Commission order APS to file a revised TEAM POA as discussed herein, no later than thirty days from the effective date of the Commission decision in this docket.

A handwritten signature in dark ink, appearing to read 'E. Abinah', with a stylized, cursive flourish extending from the end.

Elijah O. Abinah
Director
Utilities Division

EOA:All:elr\MAS

ORIGINATOR: Alexander Ibhadde Igwe

THE COMMISSION

October 24, 2019

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On this 24th day of October 2019, the foregoing document was filed with Docket Control as a Utilities Division Memorandum & Proposed Order, and copies of the foregoing were mailed on behalf of the Utilities Division to the following who have not consented to email service. On this date or as soon as possible thereafter, the Commission's eDocket program will automatically email a link to the foregoing to the following who have consented to email service.

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By:



Edna Luna-Reza
Administrative Support Specialist

1 **BEFORE THE ARIZONA CORPORATION COMMISSION**

2 ROBERT "BOB" BURNS
Chairman

3 BOYD DUNN
Commissioner

4 SANDRA D. KENNEDY
Commissioner

5 JUSTIN OLSON
Commissioner

6 LEA MÁRQUEZ PETERSON
Commissioner

7
8 IN THE MATTER OF THE APPLICATION
9 OF ARIZONA PUBLIC SERVICE
COMPANY TO IMPLEMENT A TAX
EXPENSE ADJUSTOR MECHANISM

DOCKET NO. E-01345A-18-0003

DECISION NO. _____

ORDER

**TAX EXPENSE ADJUSTOR
MECHANISM PHASE III**

11 Open Meeting
12 October 29, 2019
13 Phoenix, Arizona

14 BY THE COMMISSION:

* * * * *

15 Having considered the entire record herein and being fully advised in the premises, the Arizona
16 Corporation Commission ("Commission") finds, concludes and orders as follows:

17 FINDINGS OF FACT

18 **Background**

19 1. Arizona Public Service Company ("APS" or "Company") is a public utility
20 corporation certificated to provide electric service in the state of Arizona.

21 2. On April 10, 2019, APS filed its second supplemental application for Commission
22 approval to implement the Tax Expense Adjustor Mechanism ("TEAM") Phase III, along with
23 certain modifications to its TEAM Plan of Administration ("POA"). On August 29, 2019, Staff
24 docketed a memorandum and proposed order recommending Commission approval of the APS
25 Phase III filing, with certain modifications related to the tax savings associated with protected Excess
26 Deferred Income Taxes ("EDIT") from January 1, 2018 through September 30, 2019. In that filing,
27 Staff noted that APS did not propose any mechanism to refund accrued tax savings over the above
28 referenced period. As a result, Staff recommended that the Commission order APS to implement a

1 one-time bill credit that refunds approximately \$60 million of tax savings to its ratepayers. On
2 October 22, 2019, APS met with Staff to discuss its revised proposal regarding tax savings related
3 to protected EDIT over three years (January 1, 2018 through December 31, 2020), with emphasis on
4 amortization over the last twenty-two months. This memorandum and proposed order reflect Staff's
5 modification to its original recommendations in this proceeding.

6 3. The Commission approved a TEAM and the related POA for APS in Decision No.
7 76295, dated August 18, 2017. APS' TEAM and POA were approved in anticipation of the
8 enactment of the 2017 Tax Cuts and Jobs Act ("Tax Act" or "TCJA"), which became effective
9 January 1, 2018. The Tax Act resulted in several changes to the federal tax laws, amongst which
10 was a reduction of the Federal Corporate Income Tax Rate ("FIT") from the highest rate of thirty-
11 five percent to a flat rate of twenty-one percent. This provision impacted most utility companies'
12 revenue requirement; by decreasing federal corporate income tax expense, Accumulated Deferred
13 Income Taxes ("ADIT") and the related EDIT, amongst other cost elements.

14 4. On January 8, 2018, APS filed an application for Commission approval to implement
15 TEAM Phase I, which accounted for reduction of FIT from the highest rate of thirty-five percent to
16 a flat rate of twenty-one percent. APS reported that the impact of change in FIT resulted in a
17 decrease of \$119.074 million to its authorized revenue requirement. On March 5, 2018, the
18 Commission, in Decision No. 76601, approved Staff's recommendation to authorize APS to refund
19 its tax savings of \$119.074 million through a monthly bill credit of \$0.004912 per Kilowatt Hour
20 ("kWh") to most of its customers.

21 5. On August 13, 2018, APS filed a supplemental application for Commission approval
22 to implement TEAM Phase II related to the impacts of the Tax Act on its unprotected ADIT. APS
23 stated that implementation of the Tax Act resulted in approximately \$86.5 million of jurisdictional
24 unprotected EDIT. The Company requested that the Commission authorize it to refund the entire
25 savings over twelve months. Second, the Company requested Commission approval to change its
26 existing TEAM Phase I bill credit rate, from \$0.004912 per kWh to \$0.004194 per kWh. Finally,
27 APS requested certain modifications to its TEAM POA. On March 19, 2019, the Commission, in
28

1 Decision No. 77139, approved APS TEAM Phase II, as well as its requested modifications to both
2 the TEAM Phase I bill credit rate and the TEAM POA.

3 **The Company's Supplemental Proposals**

4 6. On April 10, 2019, APS filed its second supplemental application for Commission
5 approval to implement TEAM Phase III, along with certain modifications to its TEAM POA. The
6 Company reports that implementation of the Tax Act resulted in approximately \$881 million of
7 jurisdictional protected EDIT. APS proposes to amortize its reported \$881 million of protected
8 EDIT over 28.5 years, based on the Reverse South Georgia Method ("RSGM"). The Company
9 estimates an annual amortization of \$31 million of protected EDIT; and a decrease of \$34.452
10 million in revenue requirement, due to the impacts of gross revenue conversion factor and pertinent
11 adjustments to rate base.

12 7. APS seeks Commission approval to refund \$103.5 million of savings related to
13 protected EDIT from January 1, 2018 through December 31, 2020, in this proceeding. The Company
14 states that its proposal is predicated on the assumption that the impacts of the Tax Act will be fully
15 evaluated and incorporated in rates approved in the next rate case, to be filed by October 31, 2019.
16 APS requests Commission approval to refund \$64 million of the above savings as a one-time bill
17 credit, to account for savings accrued over twenty-two months, from January 1, 2018 through
18 October 31, 2019. The Company proposes to refund its estimated savings of \$64 million as a one-
19 time bill credit at the rate of \$0.006945 per kWh, to customers of record between August 1, 2019
20 and October 31, 2019. In other words, APS proposes to refund each customer of record, an amount
21 equal to the product of total consumption between August and October 2019 (three months)
22 multiplied by \$0.006945 per kWh. APS argues that the proposal to refund its tax savings to only
23 customers of record, between August and October 2019 (three months), is a practical approach
24 because of the complexity associated with tracking and refunding all its customers over the last
25 twenty-two months (January 1, 2018 through October 31, 2019). In order to allow for adequate time
26 to set-up a mechanism to refund its savings, APS requests that the Commission authorize it to
27 implement its one-time bill credit in the first billing cycle of December 2019. The Company
28 proposes to maintain a true-up mechanism that accounts for over/under refunded savings for future

1 consideration, in the event that it cannot locate all customers of record between August and October
2 2019.

3 8. APS also proposes to account for approximately \$39.5 million of protected EDIT
4 savings from November 1, 2019 through December 31, 2020, through a monthly bill credit rate of
5 \$0.001169 per kWh. The Company proposes to implement its first monthly bill credit in December
6 2019, for ease of administration. APS states that in the event that all savings related to the Tax Act
7 are not fully incorporated in the rates approved in its new rate case, it will file a new TEAM to
8 address the impacts of the Tax Act from January 1, 2021, subsequent to a Commission decision in
9 its next rate case filing.

10 *Normalization Rules related to Protected ADIT*

11 9. APS acknowledges that under the Internal Revenue Service (“IRS”) normalization
12 rules, Section 1561(d)(3)(B) of the Internal Revenue Code (“Code”) prescribes the Average Rate
13 Assumption Method (“ARAM”) as the default method for amortizing protected EDIT. The
14 Company states that under certain conditions and subject to IRS approval, the IRS permits adoption
15 of an alternate method known as the RSGM for amortizing protected EDIT. The IRS permits
16 adoption of the RSGM if a utility does not have adequate records to support the use of ARAM. APS
17 states that its adoption of the RSGM in this proceeding is appropriate because it lacks the requisite
18 records to support application of ARAM. APS contends that it satisfies the conditions specified for
19 adopting the RSGM under the Tax Act. The Company argues that its proposal to adopt the RSGM
20 is reasonable because it would be cost prohibitive to recreate the required records to amortize its
21 protected EDIT based on ARAM. Finally, APS claims that its adoption of the RSGM is beneficial
22 to ratepayers, since it more ratably amortizes protected EDIT over the remaining life of the related
23 regulatory assets.

24 10. APS has provided additional justification for its proposed adoption of the RSGM in
25 this proceeding. The Company, in its response to Staff’s second set of data requests, stated that
26 Section 13001(d)(2) of the Tax Act provides “that if, as of the first day of the taxable year that
27 includes the date of enactment of the TCJA, the taxpayer was required by a regulatory agency to
28 compute depreciation for public utility property on the basis of an average life or composite rate

1 method, and the taxpayer's books and underlying records did not contain the vintage account data
2 necessary to apply ARAM, the taxpayer will be treated as using a normalization method of
3 accounting if, with respect to such jurisdiction, the taxpayer uses RSGM for public utility property
4 that is subject to the regulatory authority of that jurisdiction.” APS contends that because its books
5 and the underlying records do not contain vintage account data required for ARAM and it was
6 required by the Commission to compute depreciation on its regulated utility property based on an
7 average life or composite rate method, its proposal to adopt the RSGM is appropriate and consistent
8 with Section 13001(d)(2) of the Tax Act.

9 11. APS recognizes that adoption of the RSGM is subject to IRS approval for compliance
10 with the normalization rules, and that there are severe penalties associated with violation of the IRS
11 normalization rules related to protected EDIT. As a result, APS, in conjunction with its Tax
12 Accountants, PricewaterhouseCoopers, LLP, have been engaged in preliminary discussions with
13 IRS for issuance of a Private Letter Ruling (“PLR”), to affirm if APS’s adoption of the RSGM is
14 consistent with the provisions of Section 168(i)(9) of the Code. APS reports that on May 15, 2019,
15 the IRS responded to its pre-submission conference for a PLR, indicating that it was unable to issue
16 the requested ruling. The IRS stated in its response to APS that “The situation presented in the
17 request is generally the subject of ongoing consideration for published guidance regarding the
18 treatment of excess deferred taxes under the normalization rules and sound tax administration
19 dictates that we refrain from issuing rulings on this matter until the broader questions considered in
20 the guidance project are resolved. Therefore, we decline to issue the requested ruling.”

21 12. APS continues to argue that its decision to refund tax savings related to protected
22 EDIT before obtaining a PLR is in the public interest. The Company contends that this filing is
23 predicated on its desire to timely refund all tax savings associated with the Tax Act to the ratepayers.
24 The Company further contends that this filing is prudent and beneficial to ratepayers due to the
25 uncertainties surrounding when the IRS might issue its suggested guidance and/or issue a PLR. APS
26 states that if the IRS determines that its adoption of the RSGM in this proceeding is inconsistent
27 with the normalization rules, it will recalculate both its proposed protected EDIT amortization based
28 on ARAM as well as the related bill credit rate, to address any variance with the use of the RSGM.

1 APS states that if it becomes necessary to revise its protected EDIT based on ARAM, the Company
2 will record any under recovery as a regulatory asset for future recovery in a subsequent filing or as
3 a part of its next rate case.

4 *Reconciliation with APS' 2017 Tax Return*

5 13. APS reports that there were variances between its accounting records and federal
6 income tax positions on protected and unprotected EDIT for the financial year ended December 31,
7 2017. The variances resulted in an excess protected EDIT of \$8.151 million and a negative
8 unprotected EDIT balance of \$2.626 million, for a net EDIT of \$5.525 million. APS proposes to
9 record the net reconciliation amount of \$5.525 million as part of its protected excess tax regulatory
10 liability and amortize it over 28.5 years, consistent with its proposal under the RSGM.

11 *Change to the TEAM POA*

12 14. In this proceeding, APS has modified its TEAM POA to reflect changes ordered by
13 Decision Nos. 76601 and 77139. The Company also seeks Commission approval to modify its
14 TEAM POA to include the option to hold any under/over-refunded amounts in a balancing account
15 until its next general rate case, in lieu of an annual adjustment.

16 **Staff Analysis and Recommendations**

17 15. Staff has reviewed APS's second supplemental application for Commission approval
18 to refund approximately \$881 million of tax savings related to protected EDIT over 28.5 years
19 pursuant to the RSGM. Staff also reviewed the Company's related proposal to refund approximately
20 \$103.5 million to account for savings associated with protected EDIT, from January 1, 2018 through
21 December 31, 2020. Further, Staff evaluated APS's revised proposal to refund \$64 million of
22 savings accrued between January 1, 2018 and October 31, 2019, as a one-time bill credit at the rate
23 of \$0.006945 per kWh, to customers of record between August 1, 2019 and October 31, 2019. In
24 addition, Staff evaluated the Company's proposal to refund \$39.5 million of protected EDIT savings,
25 from November 1, 2019 through December 2020, as a monthly bill credit at the rate of \$0.001169
26 per kWh. Finally, Staff reviewed the APS proposed modifications to its TEAM POA.

27 16. Staff determined that APS' proposal to refund \$64 million of protected EDIT accrued
28 from January 1, 2018 through October 1, 2019 as a one-time bill credit, at the rate of \$0.006945 per

1 kWh, to customers of record between August 1, 2019 and October 31, 2019, is reasonable. Although
2 Staff would have preferred that the benefits of the Tax Act inure to all customers from January 1,
3 2018 to date, APS's contention that it would be impractical to track and refund all customers due to
4 associated costs and customer attrition, is logical and persuasive. Staff finds that it is appropriate to
5 accept the Company's one-time bill credit rate of \$0.006945 per kWh, derived as a product of \$64
6 million divided by estimated total consumption of 9,205,638,162 kWh (August 1, 2019 and October
7 31, 2019). Staff also recommends Commission approval of the Company's monthly bill credit rate
8 of \$0.001169 per kWh, calculated based on \$39.5 million divided by total estimated consumption
9 of 33,728,949,000 kWh, from November 1, 2019 through December 31, 2020. Staff concurs with
10 APS's assumption that the impacts of the Tax Act will be fully incorporated in its next rate case.
11 Although Staff believes that the full impacts of the Tax Act will be reflected in APS's next rate case,
12 the Company's proposal to maintain a true-up mechanism and file a TEAM to account for savings
13 from January 1, 2021, is reasonable.

14 17. Staff understands that the IRS normalization rules require utilities to adopt the
15 ARAM as the default methodology for amortizing protected EDIT. Staff is equally aware that the
16 IRS Code and certain provisions of the Tax Act allow utilities to adopt the RSGM, if certain
17 conditions exist. Staff is also cognizant of APS's concerted efforts to obtain a PLR from the IRS to
18 affirm that its adoption of the RSGM is consistent with the IRS normalization rules. The
19 correspondence from the IRS to APS confirms IRS' unwillingness to issue a PLR on this matter,
20 prior to issuance of its proposed guidance on the impact of the Tax Act of protected EDIT. Finally,
21 Staff finds that APS's proposal to revise its protected EDIT amortization based on the ARAM, if the
22 IRS determines that the adoption of the RSGM is inconsistent with the normalization rules; and
23 account for any variance within the context of its next rate case or in a subsequent filing, is
24 reasonable. APS's proposal to duly account for any variance between adoption of the RSGM and
25 ARAM, and appropriately account for any variance will ensure that the full benefits of its tax savings
26 related to protected EDIT will ultimately inure to the ratepayers. Based on these facts and APS's
27 desire to timely refund all savings related to the Tax Act to its ratepayers, Staff finds that it is in the
28 public interest for the Commission to authorize APS to refund \$881 million of protected EDIT based

1 on the RSGM over 28.5 years. Staff further recommends that the Commission order APS to file a
2 copy of an IRS ruling or determination related to its adoption of the RSGM in this docket, no later
3 than within thirty days of receiving the related IRS notice. Staff further recommends that the
4 Commission order APS to file necessary revisions to its proposal in this proceeding and propose a
5 mechanism for addressing any variance if the IRS determines that adoption of the RSGM for
6 amortizing protected EDIT as approved by the Commission in this proceeding does not conform
7 with IRS normalization rules. Staff further recommends that the Commission order APS to provide
8 a detailed analysis regarding the jurisdictional impact of the Tax Act on its operations in Arizona,
9 for a comprehensive evaluation within the context of its next rate case which is due to be filed on
10 October 31, 2019.

11 *APS Proposed Changes to TEAM POA*

12 18. Staff has reviewed APS's proposed revisions to its existing TEAM POA, to
13 incorporate changes ordered by Decision Nos. 76601 and 77139. Staff also reviewed the Company's
14 proposal to modify its POA to reflect the option to hold any over/under refunded amounts in a
15 balancing account for consideration and approval in its next rate case, in lieu of filing an annual
16 adjustment report. Staff finds APS's proposed modifications to be consistent with Commission
17 Decision Nos. 76601 and 77139. Staff also finds that APS's proposal to defer any variance related
18 to the Tax Act for consideration within the context of the next rate case is appropriate. Staff
19 recommends Commission approval of APS's proposed modifications to its TEAM POA.

20 *Compliance Filings*

21 19. Staff recommends that the Commission order APS to file a copy of the IRS ruling or
22 determination related to its adoption of the RSGM in this docket, no later than within thirty days of
23 receiving the related IRS notice.

24 20. Staff recommends that the Commission order APS to file necessary revisions to its
25 proposal in this proceeding as well as propose a mechanism for addressing any variance, if the IRS
26 determines that adoption of the RSGM for amortizing protected EDIT, as approved by the
27 Commission in this proceeding, does not conform with IRS normalization rules, within thirty days
28 of an IRS notice or ruling.

21. Staff recommends that the Commission order APS to provide a detailed analysis regarding the jurisdictional impact of the Tax Act on its operations in Arizona for a comprehensive evaluation in its next rate case, within 180 days of a Commission decision in this docket.

22. Staff recommends that the Commission order APS to file a revised TEAM POA as discussed herein, no later than thirty days from the effective date of the Commission decision in this docket.

CONCLUSIONS OF LAW

1. Arizona Public Service Company is a public service corporation within the meaning of Article XV of the Arizona Constitution.

2. The Commission has jurisdiction over Arizona Public Service Company, and the subject matter of this filing.

3. The Commission, having considered Arizona Public Service Company's application and Staff's revised memorandum, dated October 24, 2019, concludes that it is in the public interest to authorize Arizona Public Service Company to refund \$881 million of protected Excess Deferred Income Taxes based on the Reverse South Georgia Method over 28.5 years.

4. The Commission further concludes that it is in the public interest to order Arizona Public Service Company to refund \$64 million of tax savings associated with protected Excess Deferred Income Taxes between January 1, 2018 and October 31, 2019, as a one-time bill credit to customers of record between August 1, 2019 and October 31, 2019, at a bill credit rate of \$0.006945 per kWh.

5. The Commission further concludes that it is appropriate to order Arizona Public Service Company to refund \$39.5 million of savings related to protected Excess Deferred Income Taxes from November 1, 2019 through December 31, 2020, at a monthly bill credit rate of \$0.001169 per kWh.

6. The Commission further concludes that it is in the public interest to order Arizona Public Service Company to modify its Tax Expense Adjustor Mechanism's Plan of Administration, subject to Staff's recommended changes, effective immediately.

...

ORDER

IT IS THEREFORE ORDERED that the Arizona Public Service Company's Tax Expense Adjustor Mechanism Phase III and the related Tax Expense Adjustor Mechanism Plan of Administration are approved.

IT IS FURTHER ORDERED that Arizona Public Service Company shall refund \$64 million of tax savings between January 1, 2018 and October 31, 2019, as a one-time bill credit of \$0.006945 per kWh, beginning in the first billing cycle in December 2019.

IT IS FURTHER ORDERED that the Arizona Public Service Company shall refund \$39.5 million of tax savings associated with protected Excess Deferred Income Taxes from November 1, 2019 through December 31, 2020, as a monthly bill credit rate of \$0.001169 per kWh, beginning in its first billing cycle in December 2019.

IT IS FURTHER ORDERED that Arizona Public Service Company shall file a copy of an Internal Revenue Service ruling or determination related to its adoption of the Reverse South Georgia Method in this docket, no later than within thirty days of receiving the related Internal Revenue Service notice.

IT IS FURTHER ORDERED that Arizona Public Service Company shall file necessary revisions to its proposal in this proceeding and propose a mechanism for addressing any variance, no later than within thirty days of receiving an Internal Revenue Service notice indicating that the adoption of the Reverse South Georgia Method for amortizing protected Excess Deferred Income Taxes, as approved by the Commission in this proceeding, does not conform with Internal Revenue Service normalization rules.

IT IS FURTHER ORDERED that Arizona Public Service Company shall file a detailed analysis regarding the jurisdictional impact of the Tax Act on its operations in Arizona, for a comprehensive evaluation within its next rate case, no later than 180 days from a commission decision in this docket.

IT IS FURTHER ORDERED that Arizona Public Service Company's proposed modifications to its Tax Expense Adjustor Mechanism's Plan of Administration are approved, subject to Staff's recommendations, effective immediately.

1 IT IS FURTHER ORDERED that Arizona Public Service Company shall file with Docket
2 Control a revised Tax Expense Adjustor Mechanism Plan of Administration, no later than thirty days
3 from the effective date of the Commission order in this docket.

4 IT IS FURTHER ORDERED that Arizona Public Service Company shall make all
5 compliance filings, as discussed herein.

6 IT IS FURTHER ORDERED that the Arizona Public Service Company shall maintain a
7 balancing account of under/over refunded amounts for consideration within the context of its next
8 rate case, in lieu of previously ordered annual adjustments.

9 IT IS FURTHER ORDERED that this Decision shall become effective immediately.

10
11 **BY THE ORDER OF THE ARIZONA CORPORATION COMMISSION**

12
13
14 CHAIRMAN BURNS COMMISSIONER DUNN COMMISSIONER KENNEDY

15
16 COMMISSIONER OLSON COMMISSIONER MÁRQUEZ PETERSON

17
18 IN WITNESS WHEREOF, I, MATTHEW J. NEUBERT,
19 Executive Director of the Arizona Corporation Commission,
20 have hereunto, set my hand and caused the official seal of this
21 Commission to be affixed at the Capitol, in the City of
22 Phoenix, this _____ day of _____, 2019.

23
24 MATTHEW J. NEUBERT
EXECUTIVE DIRECTOR

25 DISSENT: _____

26
27 DISSENT: _____

28 EOA:AII:elr/MAS

Decision No. _____

1 Arizona Public Service Company
2 Docket No. E-01345A-18-0003

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